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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In re:)	In Proceedings Under Chapter 11
BCE WEST, L.P., et al.,)	Case Nos. 98-12547 through
)	98-12570-ECF-CGC
Debtors.)	(Jointly Administered)
EID: 38-3196719)	TRIAL BRIEF OF WSG DEVELOPMENT
)	COMPANY AND LEBCON
)	ASSOCIATES REGARDING
)	ENFORCEMENT OF RESTRICTIVE
)	COVENANTS PERTAINING TO REAL
)	PROPERTY

WSG DEVELOPMENT COMPANY ("WSG") and LEBCON ASSOCIATES ("Lebcon"), parties-in-interest in these cases, by and through their counsel, Streich Lang, a Professional Association, hereby submit their joint trial brief with respect to the contested matter commenced by the Debtors' motion to determine proper purchaser filed on June 8, 1999 (the "Motion").

1 **I. INTRODUCTION.**

2 This action arises pursuant to the Motion which was filed by Boston Chicken,
3 Inc. ("Boston Chicken") and BC Real Estate Investments, Inc. (collectively, the "Debtors")
4 arising out of the Debtors' Fifth Motion to sell real property outside of the ordinary course of
5 the Debtors' business, Docket #736 (the "Sale Motion"). One of the properties to be sold
6 pursuant to the Sale Motion was designated and referred to as store #2374 located in
7 Chattanooga, Tennessee ("Store #2374"). Store #2374 is located on property which is subject
8 to various covenants and restrictions, among which is a right of first refusal ("RFR") held by
9 Lebcon (the "Property").

10 Lebcon is the owner and developer of Hamilton Place Mall Shopping Center,
11 which is the largest shopping mall in the state of Tennessee (the "Shopping Mall"). Lebcon
12 was the original owner of the Property which is adjacent to the Shopping Mall. When Lebcon
13 originally conveyed the Property in 1993, it conveyed the Property subject to various rights,
14 restrictions and covenants, all of which were designed to give Lebcon some control over the
15 ownership and use of the Property for, among other things, the preservation of the tenant mix
16 and integrity of the Shopping Mall and the preservation of the value of the adjacent property
17 which Lebcon continues to own.

18 At various times since the original conveyance from Lebcon to Donald Poole,
19 the Property has been conveyed to other grantees. At each of these times, Lebcon was
20 advised of the proposed sale and was requested to, among other things, waive the RFR. In
21 each instance, Lebcon waived the RFR, but only as to that particular sale. Two of those
22 requests (not including the request made with respect to the sale currently at issue) were
23 made by one or more of the Debtors. In addition, each conveyance of the Property after the
24 initial conveyance to Mr. Poole, has been subject to the terms and conditions of the covenants
25 and restrictions in the Deed, including the RFR. See Exhibits A through E.

1 Boston Chicken and David R. and Becky C. Smith (collectively, "Smith") entered
2 into a purchase and sale agreement dated March 23, 1999 whereby Boston Chicken agreed
3 to sell the Property to Smith upon certain terms and conditions (the "Sale Agreement"). The
4 Sale Agreement, in Paragraph 23, plainly provides that it is subject to the RFR. The Sale
5 Agreement further conditions the obligations of Boston Chicken to, among other things,
6 convey the Property to Smith, on a waiver by Lebcon of the RFR and for a termination of the
7 Sale Agreement in the event Lebcon timely exercised the RFR. Hereinafter the conditions
8 contained in Paragraph 23 of the Sale Agreement will be referred to as the "Express
9 Condition."

10 A letter dated April 2, 1999 was sent to Lebcon advising Lebcon that Smith had
11 executed a contract on the Property ("April 2 Letter"). While there is some question as to the
12 exact date that Lebcon received the April 2 Letter, there is no dispute that the April 2 Letter
13 was not accompanied by a copy of the Sale Agreement as expressly required by the Deed.
14 Lebcon finally received a copy of the Sale Agreement on April 10, 1999. However, neither the
15 April 2 Letter, the Sale Agreement, nor any other communication sent to Lebcon contained
16 a notice that a hearing would be held in this Court on April 27, 1999 at which time the Debtors
17 would sell the Property at a public sale. Moreover, at no time until the Debtors filed the
18 Motion, was Lebcon advised, by notice or otherwise, that the Debtors would attempt to sell
19 the Property free and clear of the covenants and restrictions in the Deed. In fact the opposite
20 was true since the Sale Agreement was subject to the RFR pursuant to the Express Condition.

21 A hearing was held on the Sale Motion on April 27, 1999 (the "Sale Hearing")
22 at which Smith was the successful bidder. After this Court confirmed the sale of the Property
23 to Smith, but within the forty-five day time period provided in the Deed for Lebcon to give
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1 notice of its intent to exercise the RFR, Lebcon gave notice of the exercise of the RFR.¹ The
2 Debtors thereafter filed the Motion to, among other things, determine the proper purchaser
3 of Store #2374.²

4 Despite Lebcon's timely exercise of the RFR, and, therefore, the voiding of the
5 Sale Agreement, on or about June 8, 1999, the Debtors filed the Motion. In the Motion, and
6 supporting memorandum filed June 18, 1999, the Debtors allege that there is some
7 controversy as to the proper purchaser of the Property. In fact, the Debtors allege that this
8 Court must determine whether the RFR could be avoided under a Bankruptcy Code §363(f)
9 sale or whether the RFR could be rejected, presumably as an executory contract under
10 Bankruptcy Code §365. These issues (which are, in any event, not meritorious or well
11 grounded in law or the instant facts) need not be addressed however, because the Sale
12 Agreement is controlling.

13 Even if Bankruptcy Code §§363 and 365 could have been implicated, the
14 Debtors waived whatever rights they had under these provisions by virtue of the express terms
15 of the Sale Agreement (which they drafted), including the Express Condition. Further, even
16 if there has not been a waiver of any right of the Debtors to attempt to claim any of the
17 benefits of Bankruptcy Code §§363 and 365, the Debtors have no standing or are otherwise
18 precluded from even attempting to use these Bankruptcy Code provisions to avoid or reject
19 the RFR since such an exercise would not benefit the Debtor's estate but would injure it
20 substantially.

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22 ¹ This notice was given on May 21, 1999.

23 ² On May 12, 1999, this Court approved the Sale Agreement (the "Order"),
24 including the Express Condition. The Order contains general language purporting to
25 extinguish all liens, rights and claims associated with the Property. No specific mention is
26 made of Lebcon's RFR, except in the Sale Agreement, which the Order also approved. The
specific language of the Sale Agreement takes precedence over the general language of the
Order. Given the terms of the Sale Agreement, which the Debtors drafted, the sale was
subject to the Express Condition and the inquiry should stop there.

1 For example, if the RFR was avoided under Bankruptcy Code 363(f), then
2 Lebcon would be entitled to some portion (perhaps all) of the sale proceeds in consideration
3 of the value of the interest which is being avoided.³ If the Debtors attempted to avoid the RFR
4 under Bankruptcy Code §365, then Lebcon would be entitled to a substantial damage claim,
5 if not specific performance. At a minimum, the result in either case is to diminish the net sale
6 proceeds the Debtors receive from the sale of the Property if the sale is confirmed to Smith
7 free and clear of Lebcon's interests. As a fiduciary, the Debtors have a duty to maximize
8 estate assets. As such, the Debtors have a fiduciary duty to sell the Property only to Lebcon.

9 After the sale of the Property, on or about May 21, 1999, Lebcon negotiated with
10 WSG for a sale of the Property to WSG upon certain terms and conditions. See Exhibit S.
11 While there was been innuendo that this was somehow improper, nothing could be further
12 from the truth. WSG and Lebcon freely disclosed the essential terms of the their agreement.
13 Nothing in the RFR or applicable law precludes Lebcon from agreeing to sell its interest in the
14 Property, when acquired, or assigning its interest, to a third party. Any implications to the
15 contrary or to some alleged improper actions on the part of WSG or Lebcon are irrelevant and
16 immaterial to any consideration of the matters at issue.

17 It is unclear what position the Debtors take at this point. At the initial hearing
18 held on the Motion, the Debtors indicated that they would not participate in the trial on this
19 matter, notwithstanding the fact that they initiated the matter and have filed pleadings in
20 support of awarding the Property to Smith. Moreover, since this matter is really in the nature
21 of a declaratory judgment and/or an action to determine the extent, validity and priority of an
22 interest in property, the procedural posture of this matter is questionable. However, because

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24 ³ Under Bankruptcy Code §363(f), the right to sell property free and clear is not
25 unlimited. Assuming arguendo that one of the provisions of §363(f) applied, Lebcon would
26 still be entitled to be compensated for its interest in the property which would attach to the
proceeds of the sale. In all events, Lebcon would be entitled to adequate protection of its
interest in the Property. Bankruptcy Code §363(e).

1 it is in all parties interest to have this matter resolved quickly, Lebcon and WSG are prepared
2 to proceed, notwithstanding these unusual and puzzling procedural issues.

3 **II. FACTUAL BACKGROUND.**

4 Lebcon is the original owner and developer of the Shopping Mall. It continues
5 to be substantially involved in the area as an owner, developer, manager and lessor. It owns
6 and controls substantial property interests at the Shopping Mall, including common areas and
7 other property which are directly adjacent to the Property.

8 On July 6, 1993, Lebcon conveyed the Property to Donald Poole. Beginning on
9 page 2 of the Deed (See Exhibit A), Poole, as grantee, acknowledged and agreed, on behalf
10 of himself and his successors and assigns, that the Property and his use and enjoyment of
11 the Property was subject to a variety of covenants, conditions and restrictions, including, but
12 not limited to the RFR. In fact, the RFR is but one of at least twelve (12) very specific
13 covenants and restrictions, all of which were and are designed to allow Lebcon to maintain
14 substantial control over, among other things, the use, occupancy, maintenance and control
15 of the Property and control its impact and compatibility with the surrounding Shopping Mall.
16 For example:

17 1. In subparagraph (a), there are restrictions on the manner in which the
18 property can be graded and the improvements constructed so as not to interfere with the
19 visibility of the improvements and signs located on the adjoining land (owned by Lebcon),
20 including the Shopping Mall.

21 2. In subparagraph (b), all exterior signs on the Property are to be approved
22 by Lebcon, in writing.

23 3. There are provisions regarding the obligation of the owner of the Property
24 with respect to its care and upkeep, including the requirement that any portions of the
25 Property not improved be landscaped.
26

1 4. There are restrictions on the use of the Property, including the right of
2 Lebcon to repurchase the Property if the use changes from a Kenny Rogers Roasters
3 restaurant or any other approved use. See subparagraph (f).

4 5. In subparagraph (g), page 4 of the Deed, there is a requirement that any
5 use be compatible with a first-class regional shopping center and there are certain uses which
6 are specifically prohibited such as department stores, food market, and drugstores.⁴

7 6. Subparagraph (h) on page 5 of the Deed specifically provides that the
8 covenants and restrictions are a servitude upon the Property and are to run with the land.

9 These restrictions and covenants are analogous to zoning restrictions on
10 property. Just like zoning restrictions, the restrictions and covenants in the Deed are
11 designed to control the use, occupancy and condition of the Property for the benefit of the
12 surrounding area. These restrictions are also common and customary to shopping center
13 owners and developers because they are necessary to the management and economic
14 welfare of all occupants and to ensure a synergy among occupants of a shopping center.
15 Moreover, the larger the number of occupants, the greater the delicacy and importance of
16 these land use restrictions and their enforceability.

17 Specifically with regard to the RFR, in paragraph (e) on page 3 of the Deed,
18 Lebcon is to have forty-five (45) days following the receipt of a purchase offer to exercise the
19 RFR. To commence the forty five (45) day period, the Deed requires that Lebcon actually
20 receive the proposed offer. In addition, subparagraph (e), specifically applies to the grantee
21 or its successors or assigns. In addition, subparagraph (e) makes it clear that any waiver of
22 the RFR by Lebcon as to a particular offer is not a waiver as to any future offers.

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25 ⁴ While these uses would logically be compatible with first-class regional shopping
26 centers, they were also designed to protect the integrity of the Shopping Mall. For example,
Sears and JC Penny are located in the Shopping Mall, both of which are, among other things,
department stores.

1 Through various conveyances and corporate transfers, ownership of the
2 Property was subsequently transferred to one of the Debtors. The Debtor acquired the
3 Property with actual and constructive knowledge of the RFR. First, the Deed was properly
4 recorded. Second, each of the subsequent transfers, including transfers from one of the
5 Debtors to its lender and the transfer back from its lender, are expressly subject to the terms
6 and conditions of the Deed. See Exhibits B through E. Moreover, on at least two occasions
7 prior to the attempted sale to Smith, the Debtors have sought Lebcon's consent (or waiver)
8 of the RFR with regard to the proposed transaction. Boston Chicken specifically sought
9 Lebcon's consent and waiver of the RFR for the Smith transaction, such consent and waiver
10 also being specifically required by the terms of the Sale Agreement in order for Boston
11 Chicken to have any obligation to convey the Property to Smith. Therefore, there is no issue
12 regarding the Debtors' knowledge of the existence of the restrictions and covenants on the
13 Property and the existence and enforceability of the RFR.⁵

14 On April 10, 1999, Lebcon received a copy of the Sale Agreement. Thereafter,
15 on or about May 21, 1999, Lebcon entered into a letter agreement with WSG in which Lebcon
16 agreed to: (i) exercise its RFR on behalf of WSG; or (ii) assign its RFR rights to WSG; or
17 (iii) exercise its RFR rights and then sell the Property to WSG.

18 On April 5, 1999, the Debtors filed the Sale Motion. In Sale Motion, the Debtors
19 sought to sell the Property to Smith under the terms of the Sale Agreement.⁶ The Sale
20 Agreement states that the sale to Smith is subject to Lebcon's waiver of the RFR, and that if

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22 ⁵ It is of significant importance to note that while the Debtors may now be trying
23 to convey the Property to Smith free and clear of the RFR, Smith will, in all events, take the
Property subject to the use restrictions and the right of Lebcon to approve the use of the
Property.

24 ⁶ Although Lebcon was a known party in interest, it did not receive any notice of
25 the Sale Motion or the Sale Hearing. At the initial hearing on this matter this Court noted as
26 an issue whether the principle "you snooze you lose" would apply because Lebcon had not
appeared at the Sale Hearing. There is no dispute that Lebcon did not snooze--it never had
any notice or knowledge of the Sale Hearing or any similar hearing.

1 Lebcon timely exercises the RFR, the Sale Agreement becomes null and void. There is
2 nothing in the Sale Agreement which provides for Boston Chicken or any of the Debtors to
3 convey the Property to Smith free and clear of the RFR or the other restrictions and covenants
4 running with the Property.

5 As noted, when Lebcon was given notice that Boston Chicken had entered into
6 the Sale Agreement, that notice was not accompanied by the Sale Agreement. Therefore,
7 under the specific terms of the Express Condition, the 45-day period within which Lebcon had
8 to give notice of its intent to waive or exercise the RFR did not begin to run until the express
9 terms of the RFR as contained in the Deed were complied with. That occurred on April 10,
10 1999 when Lebcon received a copy of the Sale Agreement.

11 After the Sale Hearing, on May 12, 1999, this Court entered the Order approving
12 the Sale Agreement, including the Express Condition.⁷ On May 21, 1999, well within the forty-
13 five day period provided for under the Deed after receipt of the Sale Agreement, Lebcon, on
14 its own behalf and on behalf of WSG, its designee, exercised the RFR. The timely exercise
15 of the RFR rendered the Sale Agreement null and void pursuant to its own terms.

16 Despite Lebcon's timely exercise of the RFR, and despite the Express Condition,
17 the Debtors filed the Motion contending that there is some controversy as to the proper
18 purchaser of the Property. Moreover, for the first time, it appears that the Debtors and Smith
19 are arguing that the sale was free and clear of the RFR or if it wasn't that this Court should
20 decree that it now is. However, the Debtors and Smith cannot now, by virtue of this
21 proceeding, undo what they had already agreed to, presented to this Court and provided to
22 Lebcon. In fact, one wonders why the Motion was filed in the first place, other than the
23 possibility that neither the Debtors or Smith expected Lebcon to exercise the RFR and when

24 ⁷ The Order provides, as to Store #2374, that the sale to Smith is "on the terms
25 and conditions set forth in the Motion and in the Debtors' standard form contract. The Sale
26 Motion provides that the bidding party (which included Smith) would agree to be bound by the
standard contract terms.

1 it did, they were left scrambling with what to do next. However, there is no controversy or
2 issue for this Court to decide or if there is, it is a very narrow one. The Sale Agreement has
3 been approved by this Court and is controlling of this alleged dispute. If the matter is not
4 moot, the Debtors and Smith have waived their right to argue that the sale of the Property was
5 free and clear of the RFR or any other restrictions and covenants contained in the Deed.

6 **III. LEGAL ARGUMENT.**

7 **A. Enforcing The Sale Agreement Moots All Issues.**

8 The Sale Agreement states that the sale to Smith is subject to the Express
9 Condition. Therefore, there is no justiciable issue for this Court to decide. Lebcon was given
10 notice of the offer in accordance with the terms of the Deed and within the forty-five day period
11 exercised the RFR.

12 **1. There is no controversy for this Court to decide.**

13 The Sale Agreement is subject to the Express Condition. The Sale Motion
14 provides that the sale is subject to the terms and conditions of the contract between the
15 Debtors and a purchaser. The Order approved the sale to Smith upon the terms and
16 conditions of the contract. Nowhere in the Sale Agreement is there a provision that the
17 Property will be conveyed to Smith free and clear of the RFR or any other restrictions
18 contained in the Deed. In fact, the contrary is true. Paragraph 5.2(b) of the Sale Agreement
19 specifically provides for Smith to approve the condition of title to the Property and to terminate
20 the agreement if such condition is not acceptable.⁸ Mootness occurs when "an action loses
21 its 'character as a present live controversy. . . ." Di Giorgio v. Lee, 134 F.3d 971, 974 (9th
22 Cir. 1998). Whenever an action loses its character as a live controversy, the action is moot
23 and should be dismissed. Id. In essence, there is nothing for a court to decide.

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The parties have stipulated that

1 That is the case in this matter. Only after Smith and the Debtors executed the
2 Sale Agreement with the Express Condition, only after this Court confirmed the sale subject
3 to the Express Condition did Smith and the Debtors seek relief from the very condition which
4 they agreed upon and this Court approved. Therefore, they should not now be allowed to
5 raise any issues and should be bound by their agreement, the Order and the exercise by
6 Lebcon of the RFR.⁹

7 **2. Lebcon timely exercised the RFR.**

8 The Deed grants Lebcon forty-five(45) days to exercise the RFR measured from
9 the date Lebcon is informed of an offer and receives the actual purchase agreement. In
10 relevant part, the Deed provides:

11 If Grantee or its successors or assigns receives a bona fide offer
12 (A) to purchase the [P]roperty... prior to acceptance of an Offer,
13 Grantee shall give Grantor [Lebcon] notice (the "Offer Notice")
14 **enclosing a copy of the Offer**. Grantor [Lebcon] shall have forty
five (45) days from following **receipt** of the Offer Notice to elect to
acquire the interest in the Property that is the subject of the Offer
on the terms and conditions set forth in the offer.

15 (Emphasis added.) Thus, to commence the forty five day period, Lebcon must have received
16 the Sale Agreement. Lebcon received the Sale Agreement on April 10, 1999, and exercised
17 the RFR on May 21, 1999, well within the forty-five day period.¹⁰ Accordingly, pursuant to the
18 Deed and the Sale Agreement, Lebcon is the bona fide purchaser of the Property and the
19 Sale Agreement is null and void.

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23 ⁹ It also appears that the Debtors and Smith may be trying to collaterally attack
24 the very Order which the Debtors prepared related to the Sale Agreement they prepared and
Smith freely signed.

25 ¹⁰ There is some dispute as to when Lebcon received the April 2 letter; however,
26 receipt of that letter is irrelevant since the Deed clearly provides that the time period begins
to run when Lebcon receives a copy of the offer.

1 **3. The Debtors and Smith waived all rights to avoid or reject the RFR.**

2 By entering into the Sale Agreement, and the Express Condition in particular,
3 the Debtors and Smith have waived any right they may have had to sell the Property free and
4 clear of the RFR under Bankruptcy Code §363(f) and to now claim that the sale was free and
5 clear of the RFR. In re Oyster Bay Cove Ltd., 196 B.R. 251 (E.D.N.Y. 1996) (terms and
6 conditions of approved sale agreement which specified that sale was subject to covenants,
7 restrictions and easements did not conflict with order approving sale free and clear of liens).

8 Waiver occurs when a party relinquishes a known right or exhibits conduct that
9 warrants an inference of intent to waive a right. Meineke v. Twin City Fire Ins. Co., 181 Ariz.
10 576, 581, 892 P.2d 1365, 1370 (App. 1994); Bailey v. Life & Casualty Ins. Co., 35 Tenn. App.
11 574, 584, 250 S.W.2d 99, 103 (1952). Both parties waived their right to argue that the sale
12 pursuant to the Sale Agreement was free and clear of any interest of Lebcon, including, but
13 not limited to the RFR. The Debtors and Smith agreed to the transaction and to the Express
14 Condition. No notice was given to Lebcon that there would be any attempt to sell the Property
15 free and clear of any of the restrictions, including the RFR. This Court can legitimately
16 conclude that the reason no notice was given was because the Debtors were not selling free
17 and clear of the RFR but were selling subject to the RFR in accordance with the Express
18 Condition and the Sale Agreement which they negotiated and drafted with the Smith.

19 **4. The Debtors lack standing.**

20 To the extent that this matter was initiated by the Debtors,¹¹ and the Debtors
21 seek, either through the Motion or through Smith, to persuade this Court that it should approve
22 the sale of the Property to Smith, the Debtors lack standing to do so. The Debtors' estate will
23 not be affected by a sale to Smith or Lebcon because the RFR requires Lebcon to match the
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¹¹ Again, the procedural posture of this matter is rather unusual.

1 Smith offer term for term. The Debtors, therefore, lack standing to prefer one purchaser over
2 another when its bankruptcy estate will not be affected by the outcome.

3 Under the same analysis, the Debtor lacks standing to use Bankruptcy Code
4 §363 and 365 to avoid or reject the RFR because to do so would provide no benefit to its
5 bankruptcy estate.¹² In re Wellman, 933 F.2d 215 (4th Cir. 1991) (debtor lacks standing to
6 avoid transfers where avoidance will not benefit the estate); cf. In re Bullet Jet Charter, Inc.,
7 177 B.R. 593 (Bankr. N.D. Ill. 1995) (contract cannot be rejected unless there is some benefit
8 to the estate); In re Riverside Investment Partnership, 674 F.2d 634 (7th Cir. 1982) (debtor
9 cannot sell property under Bankruptcy Code §363(f) unless there is some benefit to creditors).

10 There is no benefit, only a detriment to the estate the Debtors' creditors if the
11 sale is confirmed to Smith and the RFR is avoided in some manner. Accordingly, the terms
12 of the Sale Agreement should be honored and the Property should be sold to Lebcon which
13 is the most beneficial result to the estate.

14 **B. The RFR Cannot Be Avoided Under The Bankruptcy Code.**

15 **1. The Property may not be sold free and clear of the**
16 **RFR.**

17 The Debtors may not avoid the RFR under Bankruptcy Code §363(f). To sell the
18 Property under Bankruptcy Code §363(f), the Debtors must satisfy one of five conditions. In
19 relevant part, Bankruptcy Code §363(f) provides:

20 (f) The trustee may sell property under subsection (b) and (c) of
21 this section free and clear of any interest in such property of an
22 entity other than the estate, only if --

23 (1) applicable non-bankruptcy law permits sale of
24 such property free and clear of such interest;

(2) such entity consents;

25 ¹² If anything, the Debtors should prefer Lebcon as the proper purchaser since it
26 will not have to pay a damage claim or a portion of the sale proceeds to Lebcon. Moreover,
if the RFR is rejected, nothing in the Bankruptcy Code prohibits Lebcon from demanding
specific performance. See discussion, infra.

1 (3) such interest is a lien and the price at which
2 such property is to be sold is greater than the
aggregate value of all liens on such property;

3 (4) such interest is in bona fide dispute; or

4 (5) such entity could be compelled, in a legal or
5 equitable proceeding, to accept a money
satisfaction of such interest.

6 The RFR is not a lien, and none of the other conditions under Bankruptcy Code
7 §363(f) apply. Applicable non-bankruptcy law does not permit the sale of the Property free
8 and clear of covenants and restrictions which are validly recorded.¹³ Lebcon has certainly not
9 consented to the sale, in fact it expressly objected and neither it nor WSG had any actual
10 notice of the Sale Hearing. There has been no allegation by the Debtors that the interest is
11 in bona fide dispute. In fact the opposite can be concluded by this Court by virtue of the
12 request of the Debtors that Lebcon waive the RFR. See Exhibit L. Finally, Lebcon could not
13 be compelled in a legal or equitable proceeding to accept a money satisfaction of its interest.
14 Because land is unique and in light of the strong policy interests and considerations given to
15 restrictions and covenants which run with the land, Bankruptcy Code §363(f)(5) is simply
16 inapplicable to this type of interest. Accordingly, there is no statutory basis to avoid the RFR.
17 In re Geothermal Resources International, Inc., 93 F.3d 648 (9th Cir. 1998) (equitable power
18 of bankruptcy court does not allow court to deviate from plain meaning of statute); In re Kelly,
19 841 F.2d 908 (9th Cir. 1987) (same).

20 Because the RFR cannot be avoided under non-bankruptcy law, it cannot be
21 avoided under bankruptcy law. In re Six, 190 B.R. 958 (Bankr. M.D. Fla. 1995) (sale of estate
22 property had to be sold subject to right of first refusal); In re Wauka, Inc., 39 B.R. 734 (Bankr.
23 N.D. Ga. (Norton Jr.)(1984) (property could not be sold without allowing party to exercise right
24 of first refusal. Because holder of that right did not have notice of sale hearing, sale motion

25 ¹³ See discussion infra, regarding the issue of whether the RFR is a covenant
26 running with the land.

1 would have to be denied and bidding process would have to begin anew); In re Dean, 174
2 B.R. 787 (Bankr. E.D. Ark. 1994) (sale of debtor's interest in joint venture could not be sold
3 free and clear of restrictions contained in joint venture agreement).

4 **2. The RFR is a covenant running with the land.**

5 There has been a suggestion that the Property can be sold free and clear of the
6 RFR because the RFR is not a covenant running with the land primarily because, it is alleged,
7 it does not "touch and concern" the Property. As discussed above, there is no statutory basis
8 under the Bankruptcy Court or applicable nonbankruptcy law to sell the Property free and
9 clear of the RFR. Thus, there is no need for this Court to engage in a "touch and concern"
10 analysis. Even under this analysis however, the RFR is a covenant running with the land and
11 this Court lacks the power to sell the Property free and clear of the RFR.¹⁴

12 The Debtors and presumably Smith agree that if the RFR runs with the land, it
13 cannot be avoided under Bankruptcy Code 363(f). Under Tennessee law, a covenant such
14 as the RFR runs with the land if (i) the parties intend the covenant to run with the land; (ii) the
15 covenant touches and concerns the land; and (iii) there is privity between the parties to the
16 covenant. Griswold v. Income Properties II, 1995 Tenn. App. LEXIS (1995). It is obvious that
17 all three conditions are satisfied in this case.

18 First, the intent of the parties is demonstrated by the Deed itself. See,
19 subparagraph (h), page 5 of the Deed (Exhibit A). Second, there was obvious privity between
20 the parties to the Deed. While there has also been a suggestion that the RFR does not bind
21 the original grantee's successors and assigns because it does not refer to successors and
22 assigns in every place that it refers to the grantee, such a argument is without merit. A plain
23 reading of the Deed provides otherwise. In subparagraph (e) of the Deed, there are
24 references to the RFR remaining in force as to all subsequent offers, even if Lebcon waives

25 ¹⁴ As discussed infra, one cannot pick and choose which provisions of restrictions
26 will be enforced and which won't when they are all part of an integrated whole.

1 the RFR as to one offer. In addition, many other provisions of the Deed and the covenants
2 and restrictions contained therein refer to the grantee and his successors and assigns. It is
3 also noteworthy that the Debtors have chosen to engage in this hyper technical interpretation
4 after they (as an assignee of the original grantee) have sought Lebcon's waiver of the RFR
5 on three separate occasions. The only question therefore, is whether the RFR "touches and
6 concerns" the Property.

7 Again, the best evidence for this analysis is the Deed where it is apparent that
8 the RFR is intended to affect the use of the Property. In re Net Realty, 544 F. Supp. 759 (E.D.
9 Va. 1982) (covenant restricting use of property as first class department store runs with the
10 land); In re Fleischman, 138 B.R. 641 (Bankr. D. Mass. 1992);¹⁵ In re Jenkins, 74 B.R. 440
11 (Bankr. N.D. Ga. 1987) (covenant which is intended to restrict use of land touches and
12 concerns the land). As a practical matter what could more touch and concern the land than
13 an express land use deed restriction reserved in a shopping center lot conveyance deed by
14 the developer/owner whose very existence and viability depends on the enforceability of
15 restrictions that allow beneficial non/destructive occupancy mix within and surrounding a
16 shopping center. Moreover, as stipulated by the parties and demonstrated by the map and
17 picture (Exhibits G and N), Lebcon continues to own substantial property which is immediately
18 adjacent to the Property. In addition, Lebcon retains an easement across the Property which
19 is part of the restrictions and covenants which touch and concern the Property. Accordingly,
20 to the extent this analysis is at all relevant, the RFR cannot be avoided under Bankruptcy
21 Code §363(f) since it is a covenant that runs with the land and none of the conditions of
22 Bankruptcy Code §363(f) apply.

23
24 ¹⁵ In Fleischman, the court determined that a right of first refusal at issue in that
25 case did not touch and concern the land because it only affected ownership of the property.
26 The court stressed however, that if the right of first refusal affected use of the property such
as to preserve a shopping mall scheme or mix, then the right of first refusal would touch and
concern the land. Fleischman, 138 B.R. at 643.

1 **3. The RFR cannot be severed from the balance of the covenants and**
2 **restrictions.**

3 Smith and the Debtors apparently take the position that the Property can be sold
4 free and clear of the RFR; however, that is the only restrictive covenant in the Deed which
5 they seek to avoid. Accordingly, since the RFR is part of a number of restrictions and
6 covenants contained in the same instrument, the only way that the Property can be sold free
7 and clear of the RFR is to sever it from the rest of the restrictions and covenants in the Deed.
8 State law controls the question of construction of a contract. In re Quintex Entertainment, Inc.,
9 950 F.2d 1492, 1497 (9th Cir. 1992). The Deed relates to Tennessee real property and,
10 therefore, the contract should be construed pursuant to Tennessee law. Severability of a
11 contract is determined by the intent of the parties, as evidenced by the contract itself. In re
12 Beare Co., 177 B.R. 879, 881 (Bankr. W.D. Tenn. 1994); Penske Truck Leasing Co. v.
13 Huddleston, 795 S.W.2d 669, 671 (Tenn. 1990). In the Deed, there is no evidence of any
14 intent of the parties to make the provisions of the restrictions and covenants severable. To
15 the contrary, a fair construction of the terms and provisions of the Deed establishes that the
16 parties intended the restrictions and covenants to be construed as a whole. There is simply
17 no provision for severance nor is there any expressed or implied intent that any of the
18 provisions could be severed. Accordingly, the RFR cannot be severed from the other
19 restrictions and covenants in the Deed and the Property cannot be sold free and clear of the
20 RFR.

21 **C. The Bankruptcy Code Respects Restrictive Covenants.**

22 The Bankruptcy Code respects restrictive covenants that are imposed to
23 preserve the harmonious development of shopping centers. 11 U.S.C. §365(b)(3)(A)-(D). In
24 relevant part, these statutes provide:

25 (3) For the purposes of paragraph (1) of this subsection and
26 paragraph (2)(B) of subsection (f), adequate assurance of

1 future performance of a lease of real property in a shopping
2 center includes adequate assurance --

3 (A) of the source of rent and other consideration
4 due under such lease, and in the case of an
5 assignment, that the financial condition and
operating performance of the proposed assignee
and its guarantors, if any, as of the time the debtor
became the lessee under the lease;

6 (B) that any percentage rent due under such lease
7 will not decline substantially;

8 (C) that assumption or assignment of such lease is
9 subject to all the provisions thereof, including (but
10 not limited to) provisions such as a radius, location,
11 use, or exclusivity provision, and will not breach any
such provision contained in any other lease,
financing agreement, or master agreement relating
to such shopping center; and

12 (D) that assumption or assignment of such lease will
13 not disrupt any tenant mix or balance in such
shopping center.

14 These Bankruptcy Code provisions permit shopping mall leases to be assumed
15 and assigned only if they remain subject to all restrictive covenants. In re TSW Stores of
16 Nanuet, Inc., 34 B.R. 299 (Bankr. S.D.N.Y. 1983) (restrictive covenant must be strictly
17 enforced); In re Peterman Co., 232 B.R. 366 (Bankr. E.D. Ky. 1999) (same); In re Sun TV and
18 Appliances, Inc., 234 B.R. 356 (Bankr. D. Del. 1999) (same).

19 The RFR in this case is intended to accomplish the very same purpose as
20 expressed in §365(b)(3). Whether the RFR is a covenant running with the land, an simple
21 contract between the parties, or an executory contract, the policy as articulated by Congress
22 for the assumption of shopping center leases, should guide this Court. A lot within a shopping
23 center should not be allowed to be sold in a manner which would disrupt a tenant mix or
24 balance, particularly where the owner of the shopping center took great pains to expressly
25 reserve and enforce the land use restrictions for this very purpose. However, by attempting
26

1 to avoid and or reject the RFR¹⁶, the Debtors are seeking to disturb this policy. If the Property
2 could be sold free and clear of these type of restrictions, Bankruptcy Code §363(f) would have
3 so provided. In the absence of such a specific provision, however, this Court should be
4 guided by the policy articulated in Bankruptcy Code §365(b)(3).

5 **D. The Sale and the Order Confirming the Sale Are Voidable as a Matter of**
6 **Law.**

7 If this Court determines that the Order provides for the sale of the Property to
8 Smith free and clear of the RFR and that it is within this Court's power to effect such a sale,
9 then the Order should be voided since Lebcon did not receive notice of the Sale Motion and
10 the Sale Hearing. The Debtors knew that Lebcon was a party in interest and had an interest
11 in the Property. However, as stipulated by the parties, Lebcon never received notice of the
12 Sale Hearing.¹⁷ Accordingly, the sale cannot be confirmed and the Order should be set aside
13 if this Court determines that it can proceed with the sale to Smith. In re Ex-Cel Concrete Co.,
14 Inc., 178 B.R. 198 (B.A.P. 9th Cir. 1995); In re Center Wholesale, Inc., 759 F.2d 1440, 1448
15 (9th Cir. 1985); In re Blummer, 66 B.R. 109, 114 (9th Cir. BAP 1986), aff'd, 826 F.2d 1069 (9th
16 Cir. 1987). An order approving a sale of estate property is not valid unless the holder of a
17 right of first refusal receives actual notice and is entitled to match any bid. In re Wauka, Inc.,
18 39 B.R. 734 (Bankr. N.D. Ga. 1984) (Norton Jr.).

19 In a case strikingly similar to this matter in some respects, the Bankruptcy Court
20 analyzed the notice requirement of Bankruptcy Code §363(b)(1). In re Rounds, 229 B.R. 758
21 (Bankr. W.D. Ark. 1999). In Rounds, the trustee attempted to sell property free and clear of
22 liens and claims. A party in interest who asserted an interest in the property being sold was

23 ¹⁶ See discussion regarding whether the RFR is an executory contract, infra.

24 ¹⁷ Although WSG had knowledge (not notice) of the Sale Hearing only a few days
25 prior to the Sale Hearing, besides being irrelevant to the issues before this Court, and even
26 assuming that such knowledge constituted notice as contemplated by Bankruptcy Code
§363(b)(1) (which it did not), there is no dispute that Lebcon had neither knowledge or notice
of the Sale Hearing.

1 not given notice of the sale. The party who did not receive notice knew about the bankruptcy
2 and there was some allegation that he also knew of the proposed sale. The Bankruptcy Court
3 referenced the requirement of Bankruptcy Code §363(b)(1) that a trustee may sell property
4 only after notice and a hearing. Furthermore, as analyzed by the Bankruptcy Court, parties
5 in interest are specifically required to be noticed of a proposed sale. Rule 2002(a)(2), Fed.
6 R. Bankr. P. As the Bankruptcy Court recognized, "the notice provisions are the cornerstone
7 of bankruptcy procedure." *Id.* at 763. Basic notions of due process dictate that before a party
8 can be deprived of a property right, he must be given notice and, at least, an opportunity to
9 be heard. Lebcon was not afforded either notice or an opportunity to be heard. Therefore,
10 if this Court determines that the sale should not be confirmed to Lebcon pursuant to its valid
11 exercise of the RFR, then it still cannot award the Property to Smith. The Order must be set
12 aside.

13 **E. The RFR Is Not an Executory Contract.**

14 In the Motion, the Debtors argued that the RFR is an executory contract and
15 could be rejected by the Debtors.¹⁸ However, under controlling Ninth Circuit law, the RFR is
16 not an executory contract. Although the Debtors cited In re Coordinated Financial Planning
17 Corp., 65 B.R. 711 (9th Cir. BAP 1986) as authority for their position, the continued viability
18 of the case must be questioned in light of the Ninth Circuit's opinion In re Helms, 139 F.3d 702
19 (9th Cir 1998) with regard to options. In Helms, the Ninth Circuit determined that the
20 existence of an executory contract must be determined on a case by case basis. The Ninth
21 Circuit analyzed the option in terms of what the obligations of the parties were at the time the

22
23 ¹⁸ At the initial hearing on this matter on June 29, 1999, counsel for Smith
24 suggested that the Sale Motion and the Order had the effect of rejecting the RFR which was
25 an executory contract. Even if the RFR is an executory contract (which it is not), before it
26 could be rejected, there would have to be notice and a hearing. See Bankruptcy Code
§365(a). There was no such notice to Lebcon nor was a hearing held at which the Debtors
were required to prove that rejection was in the best interests of the estate based upon their
business judgment. Therefore, such a construction is directly contrary to the express
provisions of the Bankruptcy Code.

1 bankruptcy petition was filed. In Helms the Ninth Circuit rejected its former broad rule that all
2 options were executory contracts and stated:

3 Instead, we look to outstanding obligations at the time the petition
4 for relief is filed and ask whether both sides must still perform.
5 Performance due only if the optionee chooses at his discretion to
 exercise the option doesn't count unless he has chosen to
 exercise it.

6 Id. at 706. If the contract does not require material performance from both parties when the
7 bankruptcy petition is filed, it is not an executory contract. Id. The Ninth Circuit concluded
8 its analysis by determining that option contracts are typically not executory contracts since no
9 performance is due on the filing date. Helms, 139 F.3d at 705.

10 If an option contract is not an executory contract, the RFR cannot be an
11 executory contract either. This fact is self evident in that no performance was due by Lebcon
12 or the Debtors on the filing date. Just as the optionee referred to by the Ninth Circuit, Lebcon
13 had the discretion to exercise the RFR. At the time the Debtors' petition was filed, there was
14 nothing pending which required Lebcon to decide whether or not to exercise the RFR. Under
15 controlling Ninth Circuit law, the RFR could not have been subject to Bankruptcy Code §365.¹⁹

16 Even if the RFR is an executory contract, the Debtors could not possibly be
17 authorized to reject it under the business judgment rule which would govern any such motion.
18 In re Huang, 23 B.R. 798 (9th Cir. BAP 1982). Under the business judgment rule, rejection
19 is authorized only if there is some net demonstrable benefit to the estate. Id. In this case,
20 assumption or rejection of the RFR has no bearing upon the sale price of the Property.
21 Accordingly, rejection of the RFR would not benefit the estate, and would not be approved on
22 this basis. In re Myklebust, 26 B.R. 582 (Bankr. W.D. Wis. 1983) (if right of first refusal is
23 executory, it cannot be rejected unless there is some demonstrable benefit to the estate).

24 ¹⁹ In addition, the RFR is part of an integrated contract about which there is no
25 dispute regarding whether the provisions are executory. Therefore, since the contract must
26 be assumed or rejected as a whole and since the other provisions are not executory, the Deed
is not subject to assumption or rejection. See In re Beare Co. 177 B.R. at 881.

1 In fact, rejection of the RFR injures the Debtor's estate. If the RFR is rejected,
2 Lebcon would be entitled to a substantial damage claim,²⁰ thus increasing estate liabilities
3 without providing any benefit. The Debtors could not satisfy the business judgment rule under
4 these circumstances. In re Helms, 139 F.3d 702, 705 (9th Cir 1997) (purpose of assuming
5 or rejecting a contract is to enhance estate assets); In re Myklebust, 26 B.R. 582 (Bankr. W.D.
6 Wis. 1983) (right of first refusal could not be rejected); In re Chestnut Ridge Plaza, 156 B.R.
7 477 (Bankr. W.D. Pa. 1993).

8 **IV. CONCLUSION.**

9 The Debtors and Smith negotiated an agreement which contained the Express
10 Condition. Lebcon, as the holder of the RFR exercised the very right that was recognized by
11 the Debtors and Smith. Now Smith and, apparently the Debtors, want to redo the deal and
12 try and avoid Lebcon's rights. It is simply too late. The matter is either moot or Smith and the
13 Debtors have waived their right to now raise the issue of selling the Property free and clear
14 of the RFR. Even if this Court determines, however, that the matter is not moot or that Smith
15 and the Debtors have not waived their rights, the RFR is not severable from the other
16 provisions of the Deed and, therefore, the Property cannot be sold free and clear of the RFR.
17 Moreover, the RFR (including the other restrictions and covenants) is a covenant running with
18 the land and Bankruptcy Code §363(f) does not provide for a sale free and clear of such a
19 covenant. Neither Lebcon nor WSG ever received notice of the Sale Motion and, therefore,
20 any attempt to affect their rights is void.

21 Therefore, the Motion should be denied; Smith should be required to live with
22 the Sale Agreement; the sale should be confirmed to Lebcon or its designee, WSG, pursuant
23

24
25 ²⁰ In addition to its damage claim upon rejection, Lebcon may be entitled to specific
26 performance, which will moot any rejection. See In re West Chesnut Realty, 177 B.R. 501,
506 (Bankr. E.D. Pa. 1995); In re Walnut Associates, 145 B.R. 489, 494 (Bankr. E.D. Pa.
1992).

1 to the RFR; and this Court should grant other and further relief to Lebcon and WSG as this
2 Court deems just and proper.

3 DATED this 15th day of July, 1999.

4 STREICH LANG
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8 By /s/ Susan G. Boswell #4791
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Dated: June 22, 1999" on
file with this Court.

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5 and upon those parties listed
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7 file with this Court.

8

9 /s/ Anita Hansen

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